Postal Regulatory Commission
Submitted 11/21/2013 4:12:38 PM
Filing ID: 88345
Accepted 11/21/2013

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

Rate Adjustment Due to Extraordinary or Exceptional Circumstances

Docket No. R2013-11

PRESIDING OFFICER'S INFORMATION REQUEST NO. 11

(Issued November 21, 2013)

To clarify the Postal Service request for rate adjustments due to extraordinary or exceptional circumstances, filed September 26, 2013 (Request), the Postal Service is requested to provide written responses to the following questions. Answers should be provided no later than November 27, 2013.

1. The following questions concern workshare discounts that are below 100 percent of avoided costs.

   a. If a workshared function can be performed at a lower cost by mailers or mail service providers, please explain how the workshare discount should be structured to maximize efficiency.
   b. Please explain how efficiency is impacted when passthroughs are set below 100 percent of avoided costs.
   c. Please explain what benefits, if any, the Postal Service derives from setting passthroughs below 100 percent of avoided costs.
   d. Please explain whether it was possible to design a set of rates that generates the approximately 4.3 percent average rate increase for each product and class and also aligns these workshare discounts with avoided costs.

e. Please explain whether the Postal Service considered using its pricing flexibility to adjust discounts equal to avoided costs for workshare discounts that were set below 100 percent prior to adopting the across the board approach applied in this proceeding?

f. Please explain what consideration, if any, was given to workshare discounts not set at 100 percent of avoided costs in the Postal Service's determination that the rates proposed in this docket are reasonable and equitable.

2. The following questions concern workshare discounts that are above 100 percent of avoided costs.

g. Please explain whether it is possible to design a set of rates that generates the approximately 4.3 percent average rate increase for each product and class and also aligns these workshare discounts with avoided costs.

h. Please explain whether the Postal Service considered using its pricing flexibility to adjust discounts to equal avoided costs for workshare discounts that were set above 100 percent prior to adopting the across the board approach applied in this proceeding.

3. In Docket No. R2013-10, the Postal Service used the "rate shock exception" to explain why it was maintaining passthroughs greater than 100 percent for First-Class Automation 5-digit Flats and Standard Mail Nonautomation 5-digit Nonmachinable Letters. In light of the above CPI prices increases proposed in this proceeding, please explain why the Postal Service did not use this opportunity to align these discounts with their avoided costs.

4. In Periodicals and Standard Mail, the Postal Service has added FSS prices and is now requiring FSS preparation for mail that destinates in FSS zones.

i. Does providing discounts for Carrier Route mail sorted to the FSS send efficient price signals to mailers?

j. Please explain the rationale for providing Carrier Route discounts for mail sorted to the FSS.

5. In this docket, the proposed barcoding discount for Qualified Business Reply Mail Letters and Qualified Business Reply Mail Cards is set at different levels even though the avoided costs are the same for the two categories.

k. Please confirm that this is a consequence of the across-the –board approach. If not confirmed, please explain.

l. Please explain if the Postal Service plans to realign these discounts in the future.

m. Please explain, what consideration, if any, the Postal Service gave to changes in rate relationships other than workshare discounts and preferred rates when applying the across-the-board approach.

6. The following table details the Total Contribution from Market Dominant Products that did not cover cost from FY 2008 to FY 2012.

Market Dominant Products with Negative Contribution				
	Periodicals	**Standard Mail Flats**	**Other**	**Total**
FY 2008	437	218	327	982
FY 2009	642	616	467	1725
FY 2010	611	577	481	1669
FY 2011	609	643	344	1596
FY 2012	670	527	276	1473
	2969	**2581**	**1895**	**7445**

From FY 2008 to FY 2012, the Postal Service lost $7.5 billion on products that did not cover cost, including $ 5.5 billion from Periodicals and Standard Mail. How did this figure factor into the development of the R2013-11 prices?

7. In Docket No. R2013-10, the Postal Service proposed a new category for First-Class Single-Piece Metered Letters. In that docket, the Postal Service proposed a price for First-Class Single-Piece Stamped letters that is 1 cent higher than the price for First-Class Single-Piece Metered Letters. The Postal Service proposes to maintain the 1-cent differential between Single-Piece Stamped and Metered letters in its exigency filing. Pages 14-15 of Witness Taufique's testimony state that the 1-cent lower price for Metered letters “will mitigate the impact of the increases for small businesses.”

   a. What percent of small businesses are expected to pay the Metered versus the Stamped letter rates?

   b. How will the 1-cent differential in prices for Stamped and Metered letters mitigate the impact of the rate increases for small businesses specifically?

   c. What was the rationale for maintaining a 1-cent differential between the prices for Stamped and Metered letters in this proceeding?

8. On June 19, 2013, Valpak provided the Postal Service with its revised Standard Mail Contribution Maximization model (Valpak model).

   a. Did the Postal Service use the Valpak model in developing the rates noticed in Docket Nos. R2013-10 and R2013-11? If yes, please explain how it was used.
   b. If the Valpak model was not used, please explain why not.
   c. Please identify flaws, weaknesses, or shortcomings, if any, of the Valpak model.

9. Mr. Taufique’s statement (p. 6) lists eight classes and products that did not cover their attributable costs, according to the FY 2012 ACD. It also contains the following statement: “As urgent as the Postal Service’s financial needs are,

increases that are too high could threaten the financial health and, possibly, even the survival of **key customer segments and industries**." (emphasis added).

a. Does the Postal Service consider catalog mailers a "key segment" in the context of the statement above?

b. Please explain in more detail the link between the catalog industry and the products they use, *e.g.* Standard Mail Flats and Carrier Route?

c. What is the percentage of Standard Mail Flats and Carrier Route Flats pieces that are mailed by the catalog industry?

d. In Mr. Taufique's testimony, he notes that significant price increases could endanger the health of some customer segments and industries. Is he referring to the catalog industry with that statement? If not, or if his statement encompasses other customer segments, please list which customer segments is he referring to.

e. What research has the Postal Service conducted to identify what level of price increase would constitute a threat to the financial health of the catalog industry? Please discuss the specifics of the research conducted.

10. In Mr. Taufique's statement, he opined that an across-the-board-price increase balances many considerations and is reasonable and equitable.

a. Please explain how the cross-subsidy of underwater classes and products by other classes and products factored into the Postal Service's pricing decisions proposed in this docket.

b. What research did the Postal Service conduct into economic considerations that private sector firms factor into their pricing decisions (*e.g.* coverage, elasticity)?

c. Is comparing the approach to pricing decisions made by private sector firms to those of the Postal Service appropriate? Please explain.

11. The following table is adapted from Witness Nickerson's workpapers:

	Periodicals	**Standard Mail Flats**	**Other**	**Total**
FY 2013	499	318	44	**861**
FY2014 AR	383	186	19	**588**

a. Did Mr. Taufique work in conjunction with witness Nickerson or his staff to design prices that would minimize the amount of contribution lost by products that do not cover costs?

b. In FY 2014, Periodicals and Standard Mail Flats are projected to lose over $550 million in contribution.

   i. Did the Postal Service analyze what price increases would be required for Periodicals to be projected to cover cost in FY 2014? If so, what increase would be required?

   ii. Did the Postal Service analyze what price increases would be required for Standard Mail Flats to be projected to cover cost in FY 2014? If so, what increase would be required?

c. When does the Postal Service project that it will be able to recover sufficient revenue to cover costs of Periodicals and Standard Mail Flats?

12. In FY 2012, the average revenue per piece for Periodicals was 25.7 cents per piece, the lowest since FY 2009. The cost per piece has increased over the same period to 35.6 cents per piece.

The following table contains the Periodicals unit cost and revenue projections from witness Nickerson's Statement.

Periodicals Unit Cost and Revenue (cents)		
	Cost	**Revenue**
FY 2012	35.6	25.7
FY 2013	33.9	26.1
FY 2014 BR	33.8	26.4
FY 2014 AR	33.9	27.4

a. When developing the R2013-11 prices for Periodicals, did Mr. Taufique review the cost and revenue projections of witness Nickerson?

b. Witness Nickerson projects that Periodicals unit revenue will increase and unit cost will decrease in FY 2013, departing from the trend since FY 2009. Did Mr. Taufique design prices with this change of course in mind?

13. In witness Nickerson's Attachment 17, the test year after rate figures (January 26, 2014 implementation) show expected operating revenues of $67.2 billion (total revenues less interest and investment income) and expected controllable operating expenses of $66.7 billion (total expenses less the $5.7 billion RHB payment), resulting in an expected operating net income of $500 million. Assume that (1) the Postal Service attains the expected test year after rates volume, (2) volumes do not decline in future years, (3) wage rates do not change in future years, (4) other variable unit expenses do not change in future years, (4) no CPI-U price increases in future years, and (5) competitive products continue to produce sufficient revenue to cover at least 5.5 percent of institutional operating expenses (operating expenses here mean expenses which pertain to operations and over which the Postal Service has control. Operating expenses exclude workers' compensation non-cash adjustments and the annual payment to the postal service retiree health benefits fund).

a. Under these assumptions, would the rates requested in this case, be sufficient to cover institutional operating expenses in future years? If not, please explain.

b. Assume that volumes continue to decline, but that the other assumptions above hold. Please explain how the Postal Service will continue to cover institutional operating expenses? If not, please explain.

c. Assume that (1) volumes continue to decline, (2) the Postal Service adjusts market dominant prices annually using its price cap authority, but (3) the other assumptions above hold. Would the annually adjusted rates continue to allow the Postal Service to cover institutional operating expenses as long as the contribution lost from the volume decline was offset by the allowable price cap rate increase? If not, please explain.

d. With reference to subpart c, if the allowable price cap increase did not offset the lost contribution from the volume decline and if Congress did not permit the Postal Service to reduce delivery frequency, would the Postal Service aggressively seek to reduce institutional operating expenses in other cost segments (i.e., other than cost segments 7 and 10)? How would the Postal Service reduce these other institutional operating expenses in a way that would offset the lost contribution from declining volumes? Please describe any pragmatic limitations involved in making your decisions.

Ruth Y. Goldway
Presiding Officer